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AGENDA ITEM 3-B

TO: MEMBERS OF THE HEALTH BENEFITS COMMITTEE

- I. SUBJECT:** Legislative Proposal—
Pre-funding Retiree Health Care Benefits
- II. PROGRAM:** Legislation
- III. RECOMMENDATION:** Staff recommends that CalPERS sponsor legislation to provide specific authority to the CalPERS Board to offer a Prefunding Plan to public entities that do not participate in PEMHCA and to make other statutory changes regarding the administration of the Prefunding Plan.

IV. ANALYSIS:

This proposal would amend the law to grant the Board authority to allow public entities that are eligible to participate in PEMHCA to contract with CalPERS to participate in a Prefunding Plan, as defined, in order to pre-fund retiree health care benefits consistent with the financial disclosure requirements of the Governmental Accounting Standards Board Statements No. 43 and 45. In addition, the proposal would make other changes regarding the administration of the Prefunding Plan as set forth in this item.

Background

History of Existing Annuitants' Health Coverage Fund

In recognition of the increasing costs of retiree health care and the practice of funding such health care on an annual pay-as-you-go basis, the California Legislature established the Annuitants' Health Care Coverage Fund (AHCCF or Prefunding Plan) in 1988 to facilitate the establishment of a Prefunding Plan to pre-fund health care benefits coverage for annuitants covered by PEMHCA. While the framework was established, and while there has been ongoing discussion about how best to set up and administer a pre-funding program, the Legislature did not appropriate any money and to date no such program has been initiated.

Governmental Accounting Standards Board (GASB)

The GASB is a non-profit organization that formulates accounting standards for state and local governments. GASB standards are not law but are accounting principles that improve the relevance of financial reporting.

Statement No. 43 of the Governmental Accounting Standards Board (GASB 43), entitled "Financial Reporting for Post employment Benefit **Plans** Other Than Pension Plans", would apply to CalPERS as the administrator of a plan that is required to comply with GASB 43 uniform standards of financial reporting for other post employment benefit plans. Once CalPERS begins receiving employer contributions to pre-fund retiree healthcare benefits, CalPERS must report information about the assets on hand and the funding progress in financial statements for periods beginning after December 15, 2005, i.e., for fiscal year July 1, 2006 through June 30, 2007.

Under GASB 45, all governmental employers must report information about their funding progress and assets on hand if any or produce financial statements that are not in compliance with GASB 45 thereby receiving qualified auditor opinions. The commencement date for required disclosures for employers under GASB 45 depends on the size of the employer. Larger employers must start recognizing their liability for financial reporting periods beginning after December 15, 2006, i.e., for fiscal year July 1, 2007 through June 30, 2008.

The Board's Efforts to Assist Contracting Agencies with GASB Compliance

The CalPERS Board has directed staff to implement a three phased approach to assist Contracting Agencies in becoming compliant with GASB 45. The Board has, also, approved an increase in the Contracting Agencies' Contingency Reserve Fund (CRF) Administrative Fee from the proposed rate of 0.27% to 0.44% for Fiscal Year 2006/2007 to provide the necessary funding to implement the first phase and study the other phases of the approach. As the CalPERS Board and staff continue to work toward that end, this legislative proposal would be reflective of that effort.

Discussion

Participation in the Prefunding Plan

Under current law, only employers who have elected to participate in PEMHCA are eligible to participate in the Prefunding Plan. While CalPERS was charged with annually determining and providing to all employers participating in PEMHCA the annual rate of contribution for each employer providing benefits, whether or not they participate in the Prefunding Plan, in the past the Legislature had not appropriated the funds to allow CalPERS to comply with this charge.

The adoption of new accounting requirements for plan sponsors and for employers has provided the impetus to move forward with a Prefunding Plan. This proposed legislation adds provisions which will facilitate the establishment and administration of the Prefunding Plan and expand the group of employers eligible to participate.

Proposed Changes

This proposal would make the following changes in existing law:

- Allow public agencies that are eligible to become participants under PEMHCA, to participate in the Prefunding Plan by contract, upon board approval.
- Provide that each participating employer will be responsible to pay an amount for costs of administration.
- Add a definition of "Prefunding Plan" to mean the Annuitants Health Care Coverage Fund which is a trust fund intended to meet the requirements of Internal Revenue Code Section 115.
- Add definitions of "annuitant", "employer", "employee", and "participating employer".
- Remove the requirement that the board make an annual determination of the contribution rate for all employers under PEMHCA, replacing it with a provision that the board may rely on information provided by the participating employer if the information satisfies standards and requirements established by the board.
- Set forth the conditions under which participation in the Prefunding Plan terminates.
- Specify the order of disbursement of assets in the event of dissolution of the Prefunding Plan.
- Authorize the board to adopt regulations to implement the Prefunding Plan.

Legislative History

1988 Chapter 331 (AB 1104, Elder) – Established the Annuitants' Health Care Coverage Fund for the purpose of pre-funding health coverage for annuitants. *CalPERS Position: Sponsor*

2004 Chapter 69 (SB 626, Senate PE&R Committee) – Recodified the provisions of the Public Employees' Medical and Hospital Care Act in order to provide greater clarity. *CalPERS Position: Sponsor*

V. STRATEGIC PLAN:

This item is not a specific product of the Annual or Strategic Plans, but is part of the regular and ongoing workload of the Office of Governmental Affairs.

VI. RESULTS/COSTS:

Program Costs

We do not anticipate any new program costs. This proposal does not mandate that a public entity prefund retiree health care benefits, but would simply provide a public entity an option to contract with CalPERS to participate in a Prefunding Plan.

Administrative Costs

The administrative cost is unknown at this time. Staff will be developing a total cost analysis as part of Phase III that will be completed some time in the 2006/2007 fiscal year.

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